Markets, Trade Associations and Cartels: Centralised Wool Sales in Australia before 1939

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Abstract
Centralized wool auctions emerged in Australia from the 1890s under the management of regional wool broking associations. Their members, a small number of powerful wool brokers, cooperated with each other in the wake of shared social capital and a range of economic incentives. We investigate the consequences of the considerable market power available to these associations. An extensive theoretical literature on cartels and industrial organization suggests that sub-optimal outcomes are likely to result – reduced output and/or higher prices. An alternative associations literature focuses on the market-enhancing opportunities. We investigate the drivers of changes in broker charges and the constraints on the exercise of market power for associations.

Keywords
Cartels; market power; industry associations; contracts; commodity exchanges; wool market; wool broking

Introduction

The industrial revolution accelerated international trade in commodities. By the end of the nineteenth century sophisticated marketing channels linked producers of primary products and converters across the globe. Central markets specializing in the sale of meat, cotton, wool, grain, metals and tea played a vital function in the international economy. Drawing together buyers and sellers these markets found prices which cleared markets. Dealers and merchants stabilized prices by holding and liquidating stocks. Risks facing both sellers and buyers were attenuated by forward selling and futures trading. The cable and telegraph provided instantaneous transfer of information about prices and stocks to producers, dealers and manufacturers.

The institutions which owned and controlled major commodity markets possessed unusual characteristics. As large scale public enterprises came to dominate manufacturing, banking, insurance, shipping and so on, the organizations managing the world’s commodity markets remained small. They required little capital as the ‘market’ did not own or store the goods which were being sold in its auction rooms. They had few salaried executives and were governed by committees elected from amongst the members. In many respects they operated as clubs in which membership provided the opportunity to act as a broker or dealer. These bodies were not for profit organizations, they existed to provide the machinery for their members to conduct sales. The members were required to abide by a set of rules which, inter alia, set the fees charged to the sellers and bound members to exclusive dealing. In this respect, the marketing organizations were cartels, setting prices and enforcing restraints of trade.
This paper explores two seemingly contradictory views about the likely impact of these central marketing organizations through an examination of the control of the sale of Australian wool by associations of wool selling brokers. One the one hand, recent theoretical and empirical research on cooperation between economic actors within industry associations and trade associations has shown the efficiency enhancing outcomes of such collaboration. We will argue that commodity exchanges are a sub-set of trade associations which possess unusual capacity for efficiency gains through market widening, standardization of contracts, arbitration mechanisms to resolve disputes and so on. This positive view of trade associations reflects the application of a social capital perspective. Earlier studies of Australian wool selling brokers have shown the critical role of social capital in their formation and continuance. In contrast, an extensive economics literature claims that cartels exist to exploit the market power of their members. From their perspective, cartels result in sub-Pareto outcomes of higher prices and restricted output. However, economic theory cannot predict whether cartels will be long lasting as members are torn between accepting the benefits of being a member or taking those gained by cheating.1

Australia was an important participant in the world’s commodity trade from the early nineteenth century. Its’ wool was a key source of supply to the world’s woolen textile industry. As the volume of Australian wool entering world markets rose, the marketing channels connecting antipodean suppliers within northern hemisphere converters altered dramatically. The bulk of Australian wool had been send to the London market on consignment and a small amount had been auctioned locally. Local auctions quickly replaced the old consignment system from the 1890s. Thereafter wool was sold by auction at a small number of centralized markets which were controlled by trade associations of wool selling brokers. The governance of these associations was different from those of commodity exchanges in other countries.  

Australian firms which operated independently and in competition with one another in financing wool growers, providing station inputs and provisions, and as agents selling stock and station, joined together to cooperate in one activity, conducting a central wool auction.

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The paper will proceed in two sections. We will begin by reviewing the ways in which the selling brokers’ associations reduced high transactions costs associated with the sale of wool. Creating a more efficient market rested on the ability of the selling associations to impose ‘private ordering’ on all parties to the exchange. Social capital built amongst individuals engaged in the ‘wool trade’ lubricated the negotiations within and between associations of wool growers, sellers and buyers. It also facilitated acceptance by members of the selling brokers’ association of its rules and conditions of sale. The ‘private ordering’ undertaken by the associations through its rules and procedures provided a speedier and cheaper form of the protection of the rights of participants than could be achieved through the courts. The physical characteristics of wool raised the transaction costs facing buyers relative to those occurring in markets for those commodities such as cotton, grain, metals, and sugar which could be easily standardized. Buyers were frustrated by their inability to ascertain the ‘quality’ of the wool they purchased. The wool market operated in a fashion to attenuate these concerns through the preparation of wool for sale and through structuring the contract of sale in a way which permitted ex-post redress by buyers.

The third section analyses the behaviour of the wool selling brokers’ associations as cartels. Data from the Melbourne Woolbrokers’ Association permits us to track the fees and charges levied over a long period. This information suggests that this cartel did not actively exploit its market power. The prices charged for broking services increased after the formation of the cartel. However, the cartel had a strong incentive to engage in limit pricing as it faced strong counter veiling power from competitors. The market for wool selling was contestable over the whole of the period under consideration with new entrants. The lobbying by growers who felt that they had done better under the compulsory purchase of wool during World War I and the disposal of the overhang of stock by BAWRA than from the auction system posed another credible threat. Fees and charges were adjusted upwards over time. Across the board increases in fees were responses to rises in costs, particularly wages. The increase in the number of charges imposed on growers reflected new tasks being undertaken by the brokers prior to auction.

Section 2: Commodity exchanges, trade associations and efficiencies

Recent studies of trade association from a social capital perspective have shown how these bodies attenuated transaction costs. Bonding, monitoring and enforcement mechanisms arose organically through repeated interaction between members generating trust and valuable reputation. Personal connection provided trust, forbearance and flexibility which allowed transaction to be completed in the face of informational barriers and incomplete contracts. Participants in commodity exchanges developed social capital which supported inter-party negotiation and collective decision making about generating rules. The end point for these bodies was to create and enforce black letter law, a contract of sale.

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The governance structures of commodity exchanges date from the medieval canons of law merchant. Merchants developed and enforced a system of private law. Mercantile custom and expertise set the terms and conditions of sale at markets and fairs and provided for dispute resolution. Private associations were able to ‘coerce, enforce, or settle’ matters relating to exchange. While the rise of the contractarian principles of common law reduced the scope of the older forms of private law they did not supplant it. On the contrary, Jonathan Lurie argues that ‘the proliferation of associations so typical of the nineteenth century, together with the complexity of modern market transactions, made delegated legal power absolutely essential.’ It was the authority of the committees of the commodity exchanges to create rules, enforce compliance and swiftly settle disputes that generated efficiencies in market transactions.

Transaction costs in exchange were reduced by the evolution of a standard contract of sale. The apotheosis of commodity exchanges was the achievement of a ‘general acceptance [by] the trade’ of the ‘standardisation of trade and contract terms and establishment of …uniform contracts’. Rather than haggle over the terms and conditions for each purchase a standard contract ‘enabled commodity transactions to be reduced to their bare essentials of determining a mutually agreed price.’ Moreover, disputes between buyers and sellers were arbitrated under the rules of the trade association so ensuring that ‘procedures are swift, inexpensive and efficient, and decisions are made by trade members who are experts in their field...’ Both these developments permitted ‘swift dealing’, a pre-condition to managing growing volumes handled through the exchanges. The Australian wool selling brokers’ associations imposed standard terms and conditions of sale from their inception and which were uniform across all selling centres, replacing a system of multiple and inconsistent contract terms.

The wool selling brokers’ associations played another key role in enhancing the efficiency of the marketing process by reducing the number of places in which sales were conducted and coordinating the scheduling of sales between centres. All parties gained from having the largest position supply of wool on sale at one location. A fuller catalogue meant more buyers in attendance and greater competition amongst them. Buyers, many of whom traveled from Britain, Europe, the United States and Japan to Australia for the wool season, wanted to minimize the amount of time spent in any selling centre. Prior to the formation of the wool selling brokers’ association in the 1890s competing brokers organized their own sales with the result that buyers saw smaller catalogues and faced clashing viewing times and sales dates. The buyers pressed hard for all sales to take place at a central auction room with the roster for offerings by the various broking houses being organized by the association. The roster was organized prior to the commencement of the selling season and was communicated to the buyers’ associations.

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7 Lurie, Chicago Board of Trade, 22.
8 Baer and Saxon, Commodity Exchanges, 23-25.
9 Rees, Britain’s Commodity Markets, 415.
10 Baer and Saxon, Commodity Exchanges, 23-25.
12 Merrett, Morgan and Ville, ‘Industry associations as facilitators of social capital’, pages?
Competition amongst wool producing countries reflected their marketing organizations as much as the volume and quality of wool. Wool was sold at auction in Australia, New Zealand and South Africa, and by private treat in the USA and South America. An inter-war study argued that Australian system was significantly better than those of its rivals in three respects. First, Australia was more advanced in achieving co-ordination of sales between rival points of sale. The various state-based wool brokers’ associations had negotiated an effective national sales roster from the 1890s. Their ability to do so owed much to the overlapping membership of the Brisbane, Sydney and Melbourne associations. The New Zealand Wool Brokers’ Association, which was established in 1907, took the lead in scheduling sales amongst the ten selling centres. South Africa, by comparison, had no co-ordination of its selling centres before the late 1920s. Second, Australia had fewer selling centres which handled far higher volumes of wool than those in New Zealand or South Africa. Du Plessis argued that New Zealand growers received lower prices for their wool as a consequence. Thirdly, the Australian associations’ members and the buyers abstained from sales by private treaty so maximizing the flow of wool through the central auctions.

Transaction costs in wool markets were high because of the physical qualities of the product. In contrast to many other commodities whose quality could be determined by an objective measure, wool presented many problems. There were as many types of wool as there were breeds of sheep, and large variations within breeds. Wool ranged from coarse to fine, and the length of staple varied. The system of classifying wool at the time relying of physical examination of its ‘fineness, length, character, handle, appearance, colour, luster, soundness, strength, elasticity, and felting capacity’ was a highly subjective matter on which growers, brokers and buyers could disagree. Growers could opportunistically or unintentionally misrepresent their product as it was ‘classed’ in the shearing sheds. The needs of manufacturers for particular types of wool were very specific. However, they were unable to know whether it was of the quality they desired, or had been contaminated by foreign matter, or whether the buyer’s estimate of the conversion from ‘grease’ to clean weight was correct, until it can into the works.

The information asymmetries between grower and buyer about quality depressed prices. Buyers expected many of the lots offered to be ‘lemons’ whose revealed characteristics would be lower than they required. The standard of wool classing was low, particularly in sheds with small flocks. Specialist dealers and wool sorters

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17 Du Plessis, Marketing of Wool, 182.
18 Du Plessis, Marketing of Wool, 161-85.
21 Alfred Hawkesworth, who taught wool classing at Sydney’s Technical College since 1893, stated that ‘there are not many, certainly no more than 30 per cent of efficient wool classers’ in Australian Sheep and Wool: A Practical and Theoretical Treatise, Sydney, 1930, 6th edition, 493.
benefited from the opportunity to arbitrage by buying cheap wool which they then re-classed and repacked into consistent lines within wool types and sold to manufactures at higher prices. The wool selling brokers’ associations took steps to improve the information available to buyers prior to auction. Wool was weighed when it was received in store and the brokers’ wool classers examined each bale. Poorly packed or classed wool was re-classing and repacking prior to its offer at auction. Brokers also staked their reputations with the buyers by printing sale catalogues indicating the type of wool in each lot offered for sale and its estimated price. The buyers were given the opportunity to test the quality of wool by examining sample bales prior to auction and again after purchase. Any disputes about under weight bales and misrepresentation about quality were then dealt with by a pre-agreed arbitration process.

The development of an effective marketing organization for Australian wool was of significant importance to the prosperity of the pastoral industry and to the national economy which was so reliant upon it. Australia and other wool producing nations attempted to replicate the architecture of the London market in developing their own systems. Australia quickly came close and remained some distance ahead of its rivals. We argue that the ability of Australian actors to establish well functioning commodity markets rested heavily on the creation of social capital. Previous research suggests that almost complete coverage of industry members within the associations and the creation of bonding and monitoring mechanisms generated high levels of commitment to the organization by member firms. Social capital formed through the frequent face-to-face contact between members and the external stakeholders, most notably the buyers who were similarly organized, was the glue that held it all together. Over time ad hoc decisions and informal procedures became codified into more formal administration procedures. The social capital shared amongst individuals at senior levels in those firms providing marketing services to the pastoral industry was a necessary and a sufficient condition for the formation of a well functioning commodity market that minimized the transaction costs facing sellers and buyers.

Section 3: Cartels and monopoly pricing

The Australian wool selling broker’s associations were cartel, albeit a weak form of one. Most cartels were comprised of producers rather than of selling brokers. Producers’ cartels sought to increase prices and allocate reduced output amongst member firms so as to share out the increased profits. The wool selling brokers’ associations’ members agreed to charge the same price for their services and to sell by auction rather than engage in private treaties with buyers. These broker cartels, whose revenues came from sales commission and warehousing charges, wished to maximize the volume of commodity sales. The broker associations made no attempt to limit the number of members and did not impose any ‘quotas’ on the volume of business handled by its members.

The pricing model employed by the wool selling brokers participating in the central auction system was two-tiered from the formation of the associations in the 1890s. There was a commission on sales, a percentage of the sale price, paid by the growers. The wool growers paid a ‘receiving’ fee and the buyers paid a ‘delivery’ fee per pound or bale of wool entering the warehouse and sold at auction.

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22 See Hexner, *International Cartels*, 1948; Levenstein and Suslow; etc [references]
Were the charges imposed by the associations at the time of their formation higher than those prevailing when firms ran independent auctions? Alan Barnard’s seminal study of the Australian wool market in the nineteenth century suggests that it might not have been. The local market for consigning and auctioning services was never competitive. From the late 1850s the Melbourne Chamber of Commerce was the forum for negotiations between wool consignors and selling brokers about charges whose decisions were published in the Chamber’s *Journal of Commerce of Victoria*. The coming of the associations meant ‘the removal of the discussions from the dining-room to more formal settings.’ The leading firms had colluded to set prices which were then accepted by all parties. For the 30 years prior to the formation of the Melbourne Woolbrokers’ Association the selling commission remained at 1½ per cent and the receiving and delivery charges at ½d a pound.

The fees and charges set by the broker associations rose from the 1890s until the outbreak of the Second World War. We will use the records of the Melbourne Woolbrokers’ Association to track the changes to sales commissions and warehousing charges before addressing the issue of whether these increases represented price gouging by the cartel.

**Selling commissions**

The brokers’ associations immediately increased the commission on sales. In Melbourne the sales commission of 1½ per cent was retained for those growers whose wool realized more than £200. Those whose receipts were below this figure now paid 2½ per cent. The practice of setting the commission rate depending on the total value of wool sold by the grower was followed in selling centres in other states. Further adjustments were made favouring those with large flocks of sheep and discriminating against those with small flocks. In 1901 an addition tier was added, a commission of only 1¼ per cent was paid by growers with sales of over £500. In 1913 the Melbourne Association lifted rates to 3 per cent for sales under £200, to 2 per cent on sales between £200 and £500, and 1½ per cent for sales above £500. The other centres followed suit, although Brisbane and Sydney did not lift their rates on smaller sales to 3 per cent.

The commission on sales rose appreciably for those growers whose clips realised less than £200. A portion of growers still paid the 1½ per cent and a privileged few paid less between 1901 and 1913. We are able to calculate that in most states the majority of wool growers paid higher commissions of sales after the formation of the cartel. Australian had two wool markets. Queensland and New South Wales produced predominantly merino wool. Growers there had larger than average flocks, nearly 70

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26 Report of the Commonwealth Wool Inquiry Committee, Appendix 8, 83-84; and Fyfe Commission, para 599.
27 MWA, *Regulations and Conditions of Sale of Wool, Skins, Hides, Tallow & Grain*, various.
28 A number of commentators have erroneously imagined that either all growers paid the same rate of commission or that the weights between rates remained the same. See S. P. Stevens, *The Importance of Wool in Australia’s National Income*, Bureau of Agricultural Economics, Canberra, 1952, Table 1B, 8, and Table VIII, 20-22 and Fyfe Commission, para 599.
percent of flocks had more than 500 sheep in 1939. The four remaining states produced primarily cross breed wool. Only 35 per cent of growers had flocks of more than 500 sheep in 1939. The tiered commissions meant that the bulk of the growers, who sold the least wool, paid the highest rate of commission and the minority of growers who produced the majority of wool sold, paid a lower rate. A grower with 500 sheep might cut 14 bales. If the price of wool was £15 a bale he would breach the £200 receipt threshold and pay the lower commission rate. Wool prices remained low from the late 1890s until the outbreak of WWI so that in 15 of the 16 years between 1898/99 and 1913/14 that more than two-thirds of the growers would have paid the maximum rate. The strong rise in wool prices through the war, as a result of the Imperial purchase scheme and during the 1920s shifted the balance dramatically. In every year between 1915/16 and 1929/30 growers with flocks of upwards of 500 sheep would have sold enough bales to be eligible for the lower rate of commission. The collapse in wool prices during the depression reversed the position. Both smaller and larger growers faced higher commission charges in 1929/30 to 1932/33 and again in 1934/35 and 1938/39 when prices fell.

Receiving and delivery charges

From early 1890s until 1920 the receiving and delivery fees remained at ¹⁄₈d per pound in all Australian selling centres. In 1920, in the context of rising wool prices, they were doubled to a farthing per pound. They remained at that rate until the War with the exception of a ten per cent reduction to compensate for the fall in the price of wool between 1931/32 and 1937/38 selling seasons.

Supplementary charges

The costs charged by brokers for marketing wool rose significantly from the beginning of local sales up to the outbreak of WWII. All of the increase fell on the growers rather than the buyers. Brokers’ charges to growers reflected the increasing resources they were required to commit in warehouse space and in preparing wool for auction. The insistence of the buyers that they be better placed to judge the quality of the wool being presented at auction was the driving force behind this development. Wool delivered to store by smaller growers was also more likely to have been poorly classed, poorly pressed and inaccurately weighed. Buyers were more demanding in their pre-auction inspection of crossbreed wools. The preponderance of these wools in Victoria and Tasmania placed added burdens on brokers in those States. The wool brokers faced the inverse of the “20:80 rule”, where 80 per cent of growers generated 20 per cent of sales. The greater part of the brokers’ variable and fixed costs were

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29 The calculation involves using an annual series of average price per bale and finding how many bales would need to be sold to reach the trigger points of £200 and £500. These numbers are compared to the number of bales produced by flocks of 500 and 2,000 sheep, 14 and 35 respectively, as shown in Fegan, Merino Wool, 159-60. The average bale prices have been calculated from Statistical Handbook of the Sheep and Wool Industry, tables 36 and 45, 37 and 45. The proportion of flocks in each State and nationally are shown in Table 5 above.

30 In 1932, 88 per cent of Tasmania’s sheep and over 60 per cent of those in Victoria were non-merino. The Australian average was 20 per cent. Statistical Handbook of the Sheep and Wool Industry, tables 4-9, 7-8.
associated with the handling of the wool of the clients which generated the smallest share of their revenue.\textsuperscript{31}

The buyers’ associations pressed the selling brokers to improve their access to wool before the auction. The custom in London sales was that ‘on the morning of each sale the whole of the wool is inspected in the warehouses by prospective buyers.’\textsuperscript{32} Yet in the early Melbourne sales buyers were able to inspect only 15 per cent of lots of less than 50 bales. The buyers found these arrangements unsatisfactory and their association pressed hard to see greater proportions of wool on the show floor. By 1896 the brokers had given ground agreeing to significantly increase the proportion of wool on show, more than doubling it for ‘station’ clips and raising the rate to more than 50 per cent for bales which were badly pressed and/or classed. By 1901 a distinction had been drawn between crossbreed and merino wools which required that fewer sample bales of the latter. In 1908 another imposition is placed on the selling brokers in that now roughly two-thirds of cross breed bales and one-third of merino bales had to be shown with the top flap of the bale cut open or ‘capped’. The increased inspection requirements imposed costs to the brokers in that more bales had to be moved within the store, bales had to be re-sewn and, in the case of capped bales, re-sewn and re-pressed.

Other ‘costs’ associated with classifying wool prior to sale also rose appreciably over time. For instance, the Melbourne Woolbrokers’ Association agreed to display bales so ‘as far as practicable…[so] the brands, numbers and weights can be readily seen by the buyers when examining the wool’; selling brokers would provide labour on the show floor at ‘all hours’ to facilitate inspection by buyers; any wool had been ‘packed’, repacked’ or ‘reclassed’ by the brokers was to have that shown in the catalogue; and rams wool was to be catalogued separately. From the late 1920s brokers began to re-class wool received from smaller growers, and to inter-lot this wool into larger parcels of the same type of wool.\textsuperscript{33}

These additional costs were passed on the growers. The volume of work done in store, and labour needed to perform it, was a function of the total number of bales handled through the selling season and, importantly, the average size of the clip being received from growers. There were marked economies of scale arising from having a high volume of wool through the store. There were also diseconomies associated with processing a large number of small clips offered for sale. Australian Mercantile Land and Finance sold the same amount of wool in Sydney and Melbourne in 1910, but had only 675 clips in Sydney compared to the 1,768 received at Melbourne. More than half of the Melbourne clips were less than 10 bales which “forced the Company to own a much larger floor space in Melbourne than in Sydney so as to show buyers a greater proportion of the wool offered for sale.”\textsuperscript{34}

The growing volume of work being done for every bale entering in the wool stores and its changing nature had important implications for the brokers and their

\textsuperscript{31} The fixed cost element was the record keeping associated with each lot received into the store. A broker in Western Australia used 19 separate documents to track the tasks involved from the receipt of wool to its sale. \textit{Fyfe Commission}, Appendix 2, 182-3.


\textsuperscript{33} MWA, \textit{Wool-Selling Regulations and Conditions of the Sale of Wool}, various.

\textsuperscript{34} Bailey, \textit{Pastoral Banking}, 183.
workforce. More labour was needed in the stores as an increasing proportion of bales were moved up and down to the show floors, “the most expensive part of the Brokers business”. Increasingly wool was re-classed in store and similar lines of wool from small lots were combined together by inter-lotting.

The workers in wool stores, members of the Federated Storemen and Packers Union of Australia, argued successfully that their jobs were highly skilled and deserving of ‘margins’ above the minimum or basic wage. In 1923, Sir John Quick, Deputy President of the Arbitration Court, awarded very large increases in wages to men working in wool stores. Importantly, he accepted the union’s argument that more and more of the work being done constituted “special or extraordinary duties …. such as pressing wool; dumping bales of wool; stacking bales of wool; weighing, shipping and delivery work,…[and] classing wool.” His award increased the number of ‘classifications’ to which margins for skill and “increased rates of pay attached to such classifications”. He also increased the piece rates paid to men working on the wool presses and engaged in re-sewing the wool sacks of sample bales. Wages rose by more than 40 per cent between 1918 and 1923-24 for most of the jobs being done in store with the wages of wool classes, whose work was deemed to be the equivalent of wool sorting, rising by more than two-thirds.

Price gouging or protecting margins?

The price charged by the wool brokers’ associations for selling wool rose after the formation of the cartel. Were prices set by what the traffic would bear or did they reflect the pressure placed on margins by rising costs? Rising prices do not necessarily mean monopoly profits. An examination of the timing of the associations’ price rises suggests that most resulted from pressures from the buyers for them to commit more resources within the wool stores to prepare wool for auction and by increases in their wage costs. The economics of wool brokering altered significantly between the 1890s and World War II. Prior to the major shift of the sale of Australian wool from London the relatively small lots handled by local brokers required little infrastructure. Over time local brokers needed to make substantial investments in warehouse capacity as the amount of wool produced more than doubled between 1900 and 1939. Local selling brokers combined functions that were undertaken separately in London, auctioning and warehousing. Barnard notes that in London warehousing charges were more volatile than brokers’ sales commissions, the difference being the former’s sensitivity to changing labour costs and labour productivity. The tapering of the sales’ commissions is consistent with brokers compensating themselves for the diseconomies of scale when dealing with lots of small clips.

35 MWA, Minutes of joint meeting of Trade Committee and representatives of the Geelong Woolbrokers Association, 29 July 1930.
38 Federated Storemen and Packers’ Union v Amalgamated Mercantile Land and Finance Company Limited and Ors, CAR, No. 180 of 1923; CAR, No. 54 of 1924.
40 Barnard, Australian Wool Market, 115.
Many contemporary and later observers believed that the selling broker’s cartel exploited their market power by raising the price of their services. Growers, facing falling wool prices, indebtedness, drought, and plaques of rabbits looked with suspicion at the published reserves and profits of the largest firms selling wool.41 Pastoralists appearing before a Royal Commission into the Western Australian wool industry in the late 1930s complained about rising charges and inadequate rebates during the Depression.42 Their views echoed those of an earlier enquiry which charged that the selling brokers were profiteering by failing to pass on reductions in their own costs to the growers in the form of further reductions in receiving charges.43 Post-war economists deduced that the brokers possessed market power from their study of the structural characteristics of the industry, high levels of seller concentration, clients tied to broking firms as debtors and collusive behaviour amongst firms with respect to price. Ross Parish commented that ‘it would be surprising if wool selling charges did not contain a component attributable to the brokers’ monopoly power.’44

The beneficiaries of monopoly pricing were the members of the association not the body itself. Published accounts of the many firms involved in wool selling shed little light on the question. These firms were multi-product companies who made loan advances against produce and property, acted as selling brokers for real estate and a variety of produce, sold consumables and equipment to clients, operated their own stations as well as selling wool. Past and present profits were a poor proxy of whether wool growers were being overcharged for the sale of their wool.45 Valuable data about the profitability of wool broking comes from Goldsbrough Mort in the early 1930s.46 An internal report prepared compared the earnings and expenses of the Wool Departments in Sydney, Melbourne, Adelaide and Perth. Head Office lamented that usefulness of the figures was undermined by differences in their construction. There were wide variations in the figure of ‘profits per bale’ between centres between 1931 and 1933 with Melbourne averaging the highest and Perth the lowest. For Melbourne the ratio of ‘profit per bale’ to ‘expense per bale’ ranged between 25 and 33 per cent. The profit was around 1½ per cent of the selling price of a bale of wool.

Limit Pricing

Goldsbrough Mort’s snapshot of its returns to wool broking cannot answer the counterfactual question of whether the profits enjoyed by members of the cartel were greater than they would have been in the absence of the cartel. We will argue that the

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45 Fyfe Commission, paras 582-609.
46 Memo for Major Lewis in response to Head Office Private Letter No.651, 2nd August 1933.
Goldsbrough Mort, Noel Butlin Archive, accession number, document number?
selling associations did possess market power that permitted them to charge higher prices to growers and buyers than would have existed in a competitive market. But any impulse to charge prices that reflected the full extent of that monopoly position was moderated by a number of factors. These included the contestable nature of the wool broking market, the presence of viable alternative marketing arrangements such as consignment to London and government or grower controlled marketing process, and the symbiotic nature of the sellers’ relationships with both the growers and the buyers.

**Contestable markets**

The wool broking market was contestable despite the existence of barriers to entry. These included the capital requirements for wool stores, access to specialized wool experts, a strong brand identity and economies of scale coming from a high turnover through the selling season. Firms fought hard to attract and retain customers through bundling up services to clients, and using travelers to approach ‘free’ growers without ties to a rival. A newcomer would struggle to overcome what Ville has described as the form of relationship marketing practiced by the incumbent firms to forge enduring relationships with individual growers.47

Over the first four decades of the twentieth century there was modest turnover in the number of firms selling wool in the various selling centres. *Dalgety Annual Wool Review* shows 25 new firms entering the various markets.48 The entrants were comprised of established firms who established themselves in second, third or fourth selling centres, and new firms, the most important of whom were farmer cooperatives. They had developed a large franchise amongst smaller farmers in the wheat sheep belt primarily through the bulk purchase of inputs before extending their range of services.49 While the number of firms acting as sellers brokers in any market was small, only Sydney and Brisbane had more than ten, the market share of the top four firms was below 50 per cent in Sydney and fell sharply in both Brisbane and Melbourne.50 These three markets sold 60 per cent of Australian wool.

Entry necessarily eroded any monopoly profits. Given that the amount of wool coming onto the market after shearing each season was fixed, an increase in the number of competing brokers would reduce the volume handled by each of them, making a lower contribution to fixed costs. The number of firms entering the industry suggests that wool broking was seen as an ‘attractive’ industry.51 It was the practice of wool broking associations to admit any company which sought to join provided they paid the small entry fee and annual subscription, and agreed to abide by the rules. If the associations’ set fees and charges that would maximize their members’ profits from wool broking they risked attracting even more entrants to compete them away.

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49 By the mid-1930s 30 per cent of sheep in New South Wales, Victoria, South and Western Australia were pastured on wheat farms. The ratio was nearly a half in South Australia. *Statistical Handbook of the Sheep and Wool Industry*, table 25, 20.

50 *Dalgety Annual Wool Review*, various.

Breaches of agreements by association members were rare. Sydney was the market in which firms were most likely to ‘cheat’ by offering rebate. However, no firm took the step of operating its own system of auctions independently of the associations. The lack of such action can be explained in part by the high costs facing any firm behaving in this fashion. Actions of the members of the association were closely monitored and heavy penalties, including expulsion, resulted from breach of the rules. Any firm selling outside the centre auction room and its sales roster was a less attractive option to both sellers and buyers. The volume of wool on offer would be smaller and these sales would clash with those held by the selling associations. Growers seeking lower selling costs faced switching costs by breaking established relations with firms still operating within the association. The buyers association’s rules bound their members to dealing only with members of the selling brokers’ associations. Would growers and buyers have switched allegiance if the warehousing charges and commission on sales were slashed? That no members of the selling associations chose to take this step is consistent with the view that profit margins at the current rates were not excessively high.

One group of selling brokers did offer lower selling charges, the co-operatives who did not join the brokers’ associations. The co-operatives offered a rebate to their members of 20 per cent on the commission on sales. While the co-operatives increased their share of the market the associations made no attempt to match the rebate until the mid-1930s. The re-action was confined to the Sydney and Melbourne markets where the threat from the Commonwealth Wool & Produce Co-operative was greatest. Why would the association not cut price to protect market share? There were high switching costs facing clients of those firms participating in the selling associations and to members of the co-operatives. Both sets of clients were tied to their agents through provision of bundled services and, in the case of members of co-operatives, a contractual requirement for exclusive dealing. Wool growers who wished to join a co-operative to enjoy the rebate would have to buy shares to become a member. Relations between the co-operatives and the associations were most cordial. A bargain was reached whereby the co-operatives did not become members of the associations but had their wool sold through the central auction room and agreed to abide by the terms and conditions of sale set by the associations, with

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53 The Melbourne wool buyers forbade its members buying wool from “any agent …save from recognized Melbourne or Geelong Wool Selling Brokers.” The Victorian Wool Buyer’s Association, Constitution and Rules, 1921, Clause 35.
54 A reduction in the receiving and delivery charges of ten per cent had been introduced in the 1931/32 season by the National Council of Wool Selling Brokers of Australia which extended until the 1937/38. This concession was introduced to assist growers as wool prices fell. It also minimized the gap between the association and co-operative rates. Goldsbrough Mort’s records demonstrated that the cost of the rebate more than offset what it had gained in the reduction of award wages. Goldsbrough Mort, undated internal memorandum, ‘Matters to be dealt with Re. Storemen & Packers Union Case before Arbitration Court’, Noel Butlin Archive.
55 Goldsbrough Mort persuaded the Melbourne Woolbrokers’ Association to permit its members to match the rebate given by the Commonwealth Wool & Produce Co-operative when that firm began to conduct business in there in 1934. Tsokhas, Markets, Money and Empire, 153-54. Melbourne Woolbrokers’ Association, General Committee Meeting, Amendment to clause 7 of schedule, 20 April 1934.
the exception of the rebate. The unwillingness of the associations to engage in a price war is also consistent with the slimness of margins they enjoyed at the prevailing charges and costs.

Alternative marketing channels

The commitment of the selling associations to practice limit pricing would have been increased by the credible threat posed by alternative marketing channels. There were leakages at the edges of the auction system. Consignment of wool to London continued up to World War II with the large banks being actively involved. Private sales, known as ‘country buying’, took place directly between buyers and growers. The far greater threat came from the desire of many growers for a reversion to the scheme of compulsory purchase and payment of fixed prices as had occurred during World War I. Wool brokers had strong incentives not to antagonize by price gouging those same wool growers who were being urged to abandon current marketing practices. The auction system was in abeyance from 1916 until 1920. Thereafter it operated alongside the operation of a joint British-Australian company, BAWRA, which bled the outstanding war-time stock onto the market. On two occasions, 1922 and 1925, the wool brokers watched nervously as growers voted whether to continue with the status quo or adopt the continuation of a BAWRA-style system involving compulsory acquisition and the operation of a buffer stock scheme to dampen price variation. Sir John Higgins, the main proponent of such an arrangement, told the wool selling brokers that the grower controlled marketing of Australian wool could operate independently of their services.

The brokers were extremely sensitive to the reaction of the growers to any increase in fees and charges or the imposition of new fees. For instance, a Geelong broker commented that “interlotting was a most trouble-some thing, and he agreed that it should be paid for, but seeing what they [the brokers] made out of it he doubted whether it was worthwhile risking a disturbance…” The doubling of the receiving charge in 1920 was justified by “the great increase in store and over-head charges with the certainty of a large further increase in wages next month…” Within a few years, brokers were reluctant to increase charges across the board but felt “in view of the high price of wool,…they would be justified in charging for special work for special growers.” Even then charges were linked closely to the cost of provision. Melbourne brokers explained that there was “very little [profit] in it at ¾d per lb” in their charge for bulk classing, the direct labour cost was .41d and a contribution to overhead was required. Brokers moderated charges when wool prices fell. For

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57 For details of negotiations between the Melbourne Woolbrokers’ Association and the Victorian Producers Co-operative and the Commonwealth Wool and Produce Co-operative see Melbourne Woolbrokers’ Association Minutes of Trade Committee 7 October 1920 and Minutes 1 and 2 October 1934.
60 Bailey, Pastoral Banking, 222.
61 MWA, Minutes of meeting between Trade Committee and Geelong Association, 7 July, 1924.
62 MWA, Minutes General Committee, 17 September 1920.
63 MWA, Minutes of meeting between Trade Committee and Geelong Association, 7 July, 1924.
64 MWA, Minutes of meeting between Trade Committee and Geelong Association, 7 July, 1924.
instance, in 1930 charges for bulk classing and re-classing low grade wools were reduced because such wool “cannot at present stand the full cost of ¾d per lb.”

Symbiotic relationships with growers and buyers

Wool selling brokers might have been expected to show forbearance in their dealings with growers because of the nature of the commercial ties between them. The broking companies’ fortunes waxed and waned with those of the farm sector. A prosperous farming community, one which foresaw opportunities which necessitated borrowing, acquiring grazing land and livestock, having produce and stock to sell, offered far better prospects to the stock and station agents than one with low incomes and farmers leaving the land. Gouging on one of the many services they provided would harm their valuable reputation with clients. Squeezing wool growers might mean higher marketing margins but it might also mean the loss of a much larger connection if the client went to the wall. Stock and station agents offered many clients relief on outstanding debts during hard times in the 1890s and again in the 1930s rather than foreclose on a property whose market value was less than the book value of the outstanding loan and interest.

The wool buyers exercised considerable power in the marketing relationship. The contingent of foreign buyers who traveled to Australia for the annual sales represented their principles in a number of wool producing countries. They could switch to other markets if they were being gouged in Australia. It was the associations of buyers who were the architects of the centralized auction system forcing brokers selling independently to join as one. The state-based associations of buyers which negotiated with the brokers’ associations were well organized and used the threat of boycotts of sales in one centre while attending sales in another to force concessions on many issues, particularly relating to the inspection of wool prior to auction. On occasion, the brokers believed that their demands were excessive but did not have the bargaining power to push back. Their presence in all selling centres ensured a convergence in terms of the levels of service offered by the selling associations and their fees.

Section 4: Conclusion

Our contention is that the wool brokers’ association provided major benefits to both the growers and buyers. Efficiencies came from a form of marketing which enabled ‘swift dealing’. A reduction in the number of selling centres across the country and a co-ordinated series of sales brought the greatest number of buyers to sales with large lots on sale. Haggling between buyers and sellers was minimized by the development of a standard contract of sale and a swift and enforceable mechanism for dispute resolution. Australia had developed a superior method of selling wool compared to its main rivals, New Zealand and South Africa. It is likely that the prices received by Australian growers, for the same type and quality of wool produced in other countries,
was higher than it would have been under a series of small, competing auctions or widespread sale by private treaty.

The wool brokers’ were only partially successful in overcoming the information asymmetries that bedeviled the wool market. Buyers were given, at cost to the growers, increasing opportunities to judge the quality of wool before purchase. However, the evaluation of raw wool quality continued to be subjective until new objective measures began to be used in the 1970s.68 This inability to objectively test quality prevented the emergence of standard grades which would have allowed sale by description and the development of a futures market. Converters were able to hedge price risks through futures trading in tops, wool which had gone through the first steps of processing.69 In the absence of any hedging mechanism in the physical market for raw wool, prices remained more volatile than for cotton and synthetic fibres. Converters increased turned to blending materials to the detriment of the long term demand for wool.

The cartel increased the charges levied on growers and buyers. However, there is little evidence to support the view that they exploited all of their market power. The cartel operated by the selling brokers lacked the ability to limit, let alone reduce, the number of brokers operating within any association. The profits flowing from fixed prices were competed away by the many new entrants. Moreover, there were many factors which would lead the cartels to engage in limit pricing. Price fixing does not appear to have resulted in price gouging.